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MARKET COMMENTARY – September 2024

Quarter-End Commentary

Overview

- Major equity Indexes continued their ascent, while bonds had their second-best quarterly return in over two decades
- Australia's economy remains surprisingly resilient with continued employment strength. Annual inflation of 2.7% in August 2024, down from 3.5% in July, was the lowest reading in three years.
- Inflation is cooling, but the RBA's preferred 'trimmed mean' measure is still above target at 3.4% in August 2024

Asset class recap to end of September 2024

Global shares

The MSCI World Ex-Australia NR Index returned +4.63% over the quarter in local currency terms, with the 12-month return coming in at +30.59%. In Australian dollar terms, quarterly and annual returns were +2.30% and +23.21%, respectively, as the AUD continued to appreciate against most major currencies during Q3.

The quarter showcased a robust performance across most sectors in local currency terms:

In developed markets, the Utilities sector led the way with +15.74% over the quarter and +33.30% over the last 12 months. Information Technology was muted during Q3, returning +0.88%, however, had the strongest 12-month return at 48.63%. This points to a potential broadening of markets away from the AI thematic which has dominated year to date.

On the emerging markets front, the Chinese equity market roared back to life during Q3 delivering +22.21% in local currency terms.

The Consumer Discretionary sector was the best performing from an emerging market standpoint, up +23.44% in local currency terms during the quarter. This pushed the 12-month return of the sector to +30.31%. Like developed markets, the Information Technology sector lead the way over the previous 12-month period (+37.68%), closely followed by the Utilities sector (+34.93%).

Australian shares

Australian shares increased markedly this quarter, with the S&P/ASX200 accumulation index returning +7.79%for Q3 2024 with 12-month number returning +1.77%.

Information Technology was the strongest sector for Q3, returning +15.27%. This saw the 12-month return for the sector balloon out to +55.30%. The Consumer Discretionary (+10.61%), Materials (+10.80%) and Industrials (+10.19%) sectors all had double digit returns for the quarter with Financials (+8.30%) and Telecommunication Services (+9.66%) also posting solid returns. Energy and Utilities were the two detractors for the quarter, returning -6.38% and -1.24% respectively.

Bonds

With many central banks starting to ease monetary policy globally and yields decreasing, fixed interest assets, in general, thrived. The Bloomberg AusBond Composite 0+Y TR AUD index was up +3.02% for the quarter and +7.01% for the previous 12 months. Similarly, the Bloomberg Global Aggregate TR Hdg AUD index returned 3.99% for the quarter and 9.11% for the prior 12 months.

Global property & infrastructure

Domestic listed property (+14.30%) produced strong returns over the quarter alongside global property (+13.55%). This pushed the 12-month numbers out to +45.93% and +25.02% respectively.

Listed global infrastructure was also strong posting a return of +11.02% for Q3 and a return of +25.58% for the prior 12-months.

Currencies

The AUD was mixed across the quarter, gaining value against the USD and EUR, while losing ground against the JPY and GBP. However, given the size of the US market, broadly speaking, hedged currency exposure outperformed unhedged positions.

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Market outlook

Stocks and bonds delivered strong returns in the third quarter of 2024, defying the expectations of many investors. Major equity Indexes continued their ascent, while bonds—measured by the Bloomberg US Aggregate Bond Index—had their second-best quarterly return in over two decades. As a result, multi-asset portfolios are comfortably in positive territory for the year.

Value stocks outperformed growth stocks, small caps outpaced large caps, and non-U.S. stocks outperformed US stocks. From a sector perspective, utilities, financials, and industrials were among the top four performing sectors, while technology landed in the middle of the pack.

Strength in non-US stocks was a major development this quarter. The broad MSCI EAFE Index gained 7.3%, ahead of the S&P 500's 5.9% return. Emerging markets performed even better, advancing 8.7% in dollar terms. China, the largest component of the Index, soared by 23.5% during the quarter.

The US Aggregate Bond Index returned 5.2% in the third quarter. Emerging-market bonds and US high-yield bonds also gained, increasing by 6.1% and 5.3%, respectively. The most significant story in the bond market has likely been the actions taken by the Federal Reserve. The third quarter saw the first Fed rate cut in more than four years. The cut was widely expected, and markets have reacted positively so far, suggesting further Fed easing through year-end and into 2025.

The local market also surged to record highs in the September quarter of 2024, with the S&P/ASX 200 benchmark closing at 8,270, up 6% in three months. Financials led the charge for most of the quarter, rising despite rich valuations, although retreated somewhat in late September.

The Chinese authorities' plan for monetary and fiscal stimulus lit a fire under the materials sector, which had been the biggest underperformer in 2024. Emboldened by a potential benefit to resources demand, investors poured back into our miners, with banks funding a rotation.

The materials sector rallied hard on the stimulus news. Iron ore leaped to USD 110 per metric ton at the end of September, from USD 90 only weeks earlier and well above our long-term assumption of USD 70 per metric ton.

Economic outlook

Australia's economy is progressing toward a soft landing. Annual inflation of 2.7% in August 2024, down from 3.5% in July, was the lowest reading in three years. Temporary energy bill relief was a factor, reducing annual inflation by 0.3 percentage points on our estimates. The moderation was broader than electricity, with annual inflation falling in eight of the 11 Consumer Price Index categories. Nonetheless, monthly inflation indicators are volatile, and we look to the September 2024 quarterly inflation update, due on Oct. 30, to confirm this progress.

Restrictive monetary settings are curtailing inflation, but economic growth is anemic. Real gross domestic product rose 1% in the year to June 2024, the slowest pace since lockdown-affected 2020. Household consumption is lagging and accounts for almost 60% of economic activity. It rose only 0.5% in the year to June 2024. Interest payments weigh on consumers, and in per capita terms, June marked the sixth consecutive quarter of real GDP decline. We expect spending to pick up through fiscal 2025 as stage 3 tax cuts take effect, however, much depends on households' propensity to spend rather than save the windfall.

Despite progress on inflation, RBA Governor, Michele Bullock has made it clear the board doesn't foresee a cut before Christmas. Given the debacle of former Governor Lowe's perceived "commitment" to no hikes before 2024, it's surprising to see the RBA test the waters of forward guidance again.

The market isn't convinced by the Governor's rhetoric. Cash rate futures price a 25% chance of a cut at the November meeting and almost a 90% chance in December, the year's final meeting. The market and the Governor can't both be right. Presumably, markets are getting a steer from other central banks, many of whom have begun monetary easing. The most influential, the US Federal Reserve, did so emphatically with a 50-basis point cut in September.

Risks to global growth abound, including a possible United States recession or further turbulence in China. While the US recession is not our base case, and planned stimulus assuages near-term concerns in China, rapid deterioration on either front could force the RBA to pivot. But another hike can't be ruled out either.

Inflation is cooling, but the RBA's preferred 'trimmed mean' measure, which strips out volatile items, including fuel and electricity, is still above target at 3.4% in August 2024. Observing the experience offshore, the last mile of the inflation battle is the hardest, and any stubborn stickiness could test the market's narrative for cuts this year.